TIA White Paper

2023 Freight Outlook

TRANSPORTATION INTERMEDIARIES ASSOCIATION

CENTER OF THE SUPPLY CHAIN

2023 Freight Outlook a Delicate Balancing Act for Shippers, 3PLs, Carriers

Volatile, dislocated, tight, congested, and at times, crazy. How else would you describe supply chains from 2020 to 2022? Will 2023 be the encore performance?

An extended period of tight capacity ended in the latter half of 2022 and reset expectations for shippers, 3PLs and carriers. Inflation was throttling consumer demand. Retailers were coping with excess inventories. Shippers regained power to negotiate rates.

Balance has been returning to the freight market, but a recession could be next. In the face of uncertainty, a group of transportation and logistics executives are confident that the strategies powering success in 2022 — paying down debt, diversifying, investing in technology, strengthening relationships, and more — will deliver paybacks in the new year.

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This whitepaper from TIA focuses on impactful trends for 2023 that will cause stress for some but create opportunities for others.

Brake Lights Ahead

The freight market enters 2023 with a limp due to faltering consumer demand. Two primary factors for this are:

- **Inflation.** Consumers are purchasing fewer goods hauled by truck due to budget cutbacks and interest rates slowing construction of houses. The consumer price index (CPI) rose at historic levels in 2022. The rate of growth has slowed since June, but November ended up 7.1%, year over year.
- **Inventory drawdowns.** Retailers saw inventories surge in 2022. Supply chain disruptions made it necessary for businesses to order goods further in advance, but lower-than-expected consumer demand left retailers with a surplus that is taking time to work out.

The transportation and logistics industry has seen a widening delta between operating costs and the CPI from:

Fuel. The average retail price of diesel has been hovering at $5 per gallon since March 2022. Ongoing geopolitical tensions in Ukraine, Iran, North Korea and elsewhere could destabilize energy prices in 2023, making fuel and fuel surcharges more of a wild card.

"It is almost impossible to budget for fuel costs," said John Janson, Senior Director of Global Logistics for SanMar, a large shipper of custom apparel and accessories, headquartered in Issaquah, Wash.

Equipment. Prices for new and used tractors and trailers rose rapidly in 2021 and came down in 2022 but remained higher than normal. In September 2022, new truck prices were up 18%, year over year, according to ACT Research.

Labor. The unemployment rate entered 2023 at 4 percent. Economists consider this a fully employed market. Labor shortages will continue driving wage growth for drivers, office staff, technicians, warehouse workers and more.

Labor shortages have resulted in shipping delays and higher detention charges from carriers as well, Janson says. As well, shippers have seen major increases in the cost of supplies, packaging and chemicals. Food growers have been hit especially hard from increased fertilizer prices.

The RFP is Dead. Long Live the RFP.

All executives agree that Q1 of 2023 will be a period of downward rate adjustments for contract and spot market loads. This comes as no surprise to shippers, 3PLs and carriers, since they all have access to the same transparent rate data from industry sources.

The sources show the drop-off started in Q2 of 2022 when freight volumes slipped 2.6%, year over year, according to the U.S. Bank National Shipments Index. At the end of November 2022, the average rate per mile for truckload van transport in the U.S. spot market was $2.37, the lowest since September 2020, according to DAT Solutions.

The freight market is still growing, however. In Q3 of 2022, the seasonally adjusted freight tonnage index tracked by the American Trucking Associations was up 2.8% compared to Q3 of 2021.

Seeing a downward movement gives shipper executives reasons to conduct annual freight contracts, which have largely been missing since 2020. Spot market rates turned white hot in 2021, causing many shippers to reduce contract terms to six months or less to stabilize rates and routing guides.

Robert Savage, Vice President, Logistics and Supply Chain for Del Monte Fresh, a shipper of fresh produce, has seen rates in the company's traffic lanes fall by 25% in Q3 of 2022. The company, headquartered in Coral Gables, Fla., did six-month RFPs in 2021 and 2022 but is now conducting an annual RFP for 2023. Its new contracts will start March 15.

"I think the market will be very open. There is a lot of capacity," he says.

Quarterly RFPs were the norm in 2021 and most of 2022 for Musco Family Olives, a shipper with offices in California's Central Valley. In Q4 of 2022, the company began playing more in the spot market since rates "seem to be a little bit better than contract," says Michael Lin, Senior Director of Supply Chain. Musco is planning an annual bid for 2023.

Lin is expecting to see minor decreases in truckload rates in 2023. Intermodal rates are more likely to increase, he says. This could make it less expensive for Musco to ship containers to East

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Coast ports for inland delivery rather than ship imports to the West Coast and use intermodal services to get its freight east of the Rockies.

Intelligent Logistics, an Austin, Texas-based 3PL, is seeing more RFPs from shipper customers that have brokers and carriers bidding for the same lanes. Traditionally, RFPs separated lane bids. One consequence of this is that larger freight brokers are driving down contract bids, and it remains to be seen if they can cover those loads at the contracted price after Q1 2023, stated Brandon Arnold, Vice President of Truck Brokerage, Intelligent Logistics.

"I think we will see more lane bids come to market instead of larger or micro-type RFPs if the market does not stabilize and continues to see volatility," he continues. "Overall, we are in for an interesting Q1 and Q2 for the contract spot market, and it may take some victims with it along the way."

The Power to be Selective

With capacity expected to loosen in 2023, shippers and 3PL executives are more selective of who they do business with and are hesitant to choose the lowest cost providers in a down market.

> "The main reason for changing our thought process for 2023 is to build a proactive trusted partnership instead of a reactionary transactional relationship" he said.

The size of a 3PL's carrier database matters to shippers. They want to do business with 3PLs that have strategic partnerships with carriers. 3PLs that provide stable and consistent volumes can keep quality carriers under their loads, says Mike Mikulik, Vice President of Sales and Operations at SPI Logistics, a 3PL based in Vancouver, B.C., with more than $250 million in annual revenue.

Monin Americas, a manufacturer of food and beverage flavorings with headquarters in Clearwater, FL., traditionally held an RFP consisting of over 150 brokers. In 2023, the company will conduct an informal RFP to allocate contract and spot lanes with approximately 19 freight brokers who handled the majority of lanes over the past few years, explains J.J. Jones, Chief Supply Chain Officer.

"The main reason for changing our thought process for 2023 is to build a proactive trusted partnership instead of a reactionary transactional relationship," he said. "Another area of concern is that we still think the transportation market is more spot quote biased now and think that this will probably run through Q1 of 2023."

"By working closely with the broker partnerships, we should be able to protect and help each other as pricing decreases or if we see an increase too," Jones added.

SanMar's John Janson sees little advantage in changing transportation providers over rates. The shipper moves about 90 percent of its loads on contract. Its contracts with carriers and 3PLs include periodic rate adjustments to stay in line with movements in the spot market, up or down.

Shippers tend to favor incumbents in RFP events who have honored their contracts, especially when higher-paying loads were available in the spot market. High Tide Logistics, a 3PL with 30 employees based in Lincolnwood, Ill., is seeing customers return the favor. "They know we took losses in 2021 and 2022," says Owner Ross Schager.

High Tide Logistics is also vetting carriers more closely to avoid doing business with those who may be financially unstable, he says.

Del Monte Fresh does not invite carriers to its RFP unless they operate at least 10 trucks. The 3PLs it uses must be in business for at least five years and have more than $100 million in annual revenue. These requirements are necessary, Savage says, to protect its temperature-sensitive loads.

Historically, 3PLs move about 25% of loads but have 85% of its cargo claims. Del Monte Fresh expects 3PLs to have strategic lanes with the carriers they use to provide stable business.

"If they just do a spot quote, they're not for us," he says.

Digital Transformation

The digitization of transportation and logistics is one trend that executives are certain will continue in 2023.

Logistics executives agree that digital freight solutions like this cannot be successful without putting carriers in a strategic position to grow with them such as by providing them with back-to-back loads.

3PLs that leverage cloud-based technology, data science and API connections that make it easier for shipper customers to do business with them will have an advantage. Shippers are doing more business with 3PLs that provide real-time visibility of where capacity is, the cost, and assurance that shipments will be covered. This information can be sent directly to their transportation management systems (TMS) as "book it now" options for any lane and commodity type.

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As the transportation and logistics industry continues to move to more automation, the power of relationships will be even more important for small-to-medium 3PLs who cannot compete with the latest technology advancements. The value of getting someone on the phone to solve problems should not be underestimated, says John Miller, President of Plains Dedicated, a motor carrier and freight broker based in ChampionsGate, Fla. If drivers or shippers cannot get anyone on the phone to solve problems, "you are not going to win business," he says.

Transforming Cost Centers

Shippers who successfully managed supply chains through the turbulence of the past few years may see opportunities to leverage their physical assets and intellectual capital to transform cost centers into profit centers.

Such is the case with Tricont Logistics. About one year ago, Del Monte Fresh launched this company to do more than service its own freight. It has plans for significant growth in 2023. "Overall, we've done a good job on the logistics side," Savage says.

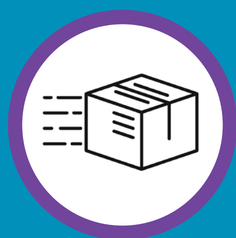
Tricont Logistics has brokerage authority. It is the parent company of Tricont Trucking, Del Monte's private fleet with for-hire operating authority, and handles billing, payroll, and other functions for both entities. The biggest customer of Tricont Logistics is and always will be Del Monte Fresh with a $230 million annual transportation spend.

Tricont Logistics also sells its freight brokerage, warehousing and distribution services to external customers with dry and refrigerated products. As well, it sells ocean freight services as well as port and container drayage with 99% on-time service.

Tricont Logistics can deliver freight from ocean to grocery stores for customers alongside its own shipments using Tricont Trucking's fleet assets. In 2022, Savage expects Tricont Logistics to bring in nearly $9 million in revenue with a possibility to be a $100 million logistics company within a few years, not counting revenue from Del Monte Fresh.

Setting Expectations

While a recession is possible in 2023, executives interviewed for this report expressed confidence in the freight market rebounding sooner rather than later. In the meantime, shippers are concerned that fuel prices will offset any savings they might be getting in truckload and LTL rates.



The good news is ***freight volumes are expected to grow.*** In December 2021, ATA released a study that forecasts continued growth in freight tonnage by **28%** between 2021 and 2032.

Profit margins for carriers and 3PLs will be squeezed, but executives are optimistic growth will continue at a moderated pace. Ross Schager from High Tide Logistics expects to do more loads in 2023 but have lower net margins per load.

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After record increases in spot and contract rates for the past two years, it will be difficult for 2023 to measure up for carriers and 3PLs. Those who used debt and private equity to finance growth in the past few years will be the hardest hit, says John Miller from Plains Dedicated.

Miller expects to see some failures of large companies in 2023 who made acquisitions in the past two years using high-interest bank notes.

"I think it will be a balanced market," he said. "If you have been frugal, paid down debt, invested in people, equipment and software, you will get through the next six months. There will be winners and losers, but I am very positive about trucking."

A special thanks to those who contributed to this report:

John Janson, SanMar
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Brandon Arnold, Intelligent Logistics
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